

HOW TO READ YORK UNIVERSITY'S FINANCIAL STATEMENTS

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York University is a not-for-profit institution that is required to issue its annual financial statements following the accounting rules set in Part III of the CICA Handbook. York's annual financial statements include four statements and the accompanying notes. The four statements are i) the Statement of Operations (SOP), ii) the Statement of Financial Position (SFP) also known as the Balance Sheet, iii) the Statement of Cash Flows (SCF), and iv) the Statement of Changes in Net Assets.

The Statement of Operations (SOP)

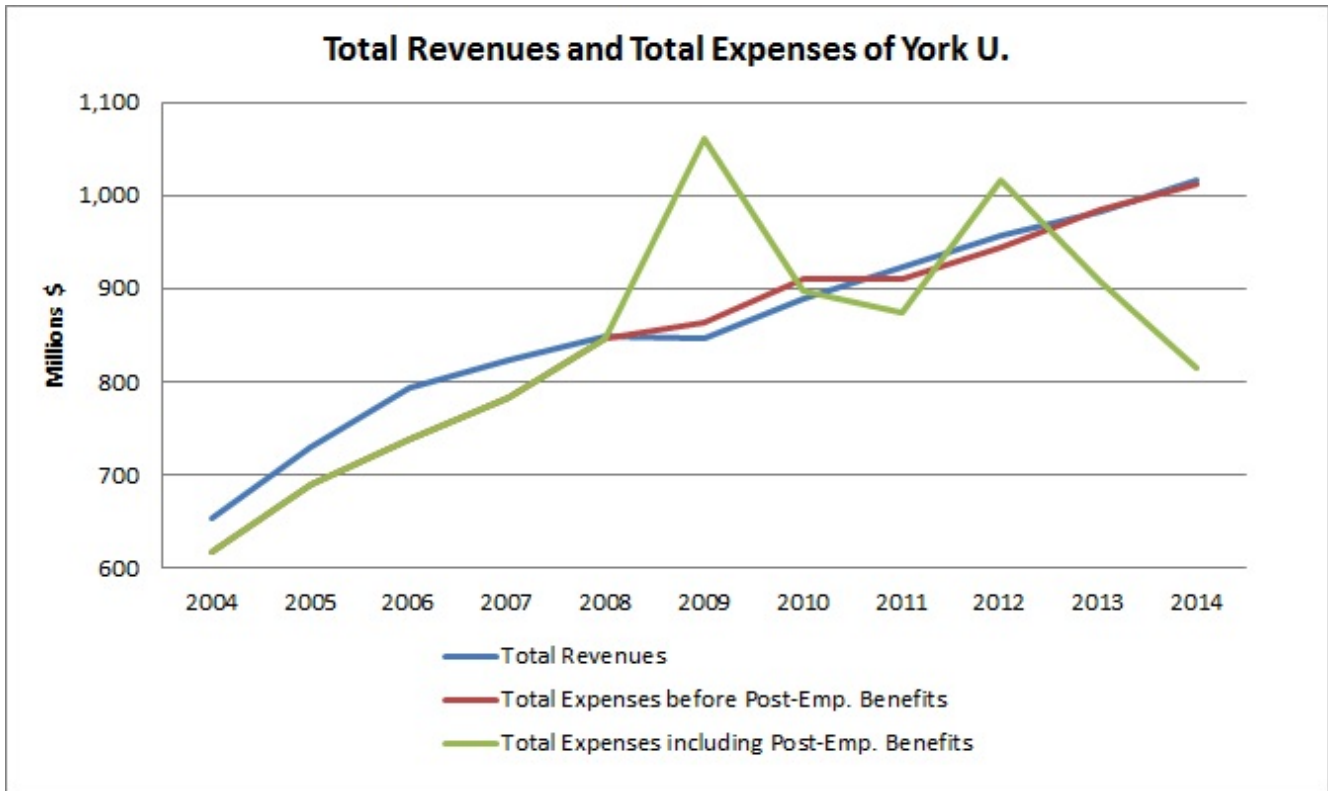
The SOP is like a movie, it records the revenues earned and their sources, and expenses incurred and their reasons during a particular period. The SOP includes revenues and expenses from/relating to bread and butter activities of an entity. For York University they would be revenues from tuition, grants, and sales, and expenses towards salaries, bursaries, and operations among other items respectively. The SOP can be represented by the equation $\text{revenues} - \text{expenses} = \text{surplus}/(\text{deficit})$. Total revenues in a particular year need not equal total cash flows from operations in that year since some of those revenues may have already been received in cash in a previous year, or will be received only in the future. Similarly, total expenses in a particular year need not match total cash flows towards operations in the year since some expenses such as depreciation expenses are non-cash expenses or some expenses were already paid for (as in pre-paid subscription expenses) or will be paid only in the future (as in expenses incurred using credit). Hence, revenues and expenses are recognized when they have been earned and incurred respectively, regardless of when the associated cash flow occurs. This is the reason why both an SOP and a Statement of Cash Flows (SCF) are needed to provide a complete picture.

For not-for-profit institutions the excess of revenues over expenses is termed a surplus, while the converse is termed a deficit. In the long run, not-for-profits should be able to finance their annual expenses and capital expenditures from operating revenues (i.e., they should break even). Hence, an occasional surplus should not be cause for jubilation nor should an occasional deficit be cause for gloom. York University swings between annual surpluses and deficits from year to year.

A snapshot of York's finances:

- 2004-2008: York generated a cumulative surplus of \$176 million *
- 2009-2014 – before considering the impact of post-employment benefit re-measurement (the change in the funded status of the pension plan over the year): York generated a cumulative deficit of \$(13) million or an average annual deficit of \$(2.6) million. This average annual deficit of \$(2.6) million represents 0.28% of the average total revenues of \$936 million during this period.
- 2009-2014 – after considering the impact of post-employment benefit re-measurement: York generated a cumulative surplus of \$41 million dollars.

* York University was not required to recognize the impact of post-employment re-measurement for 2004-2008



Note the progressively upward and roughly similar trend over time in both total revenues, and total expenses before post-employment benefits. There is no noticeable decrease in total revenues or evidence of widening operating deficits over time.

The Statement of Financial Position (SFP) – aka the Balance Sheet

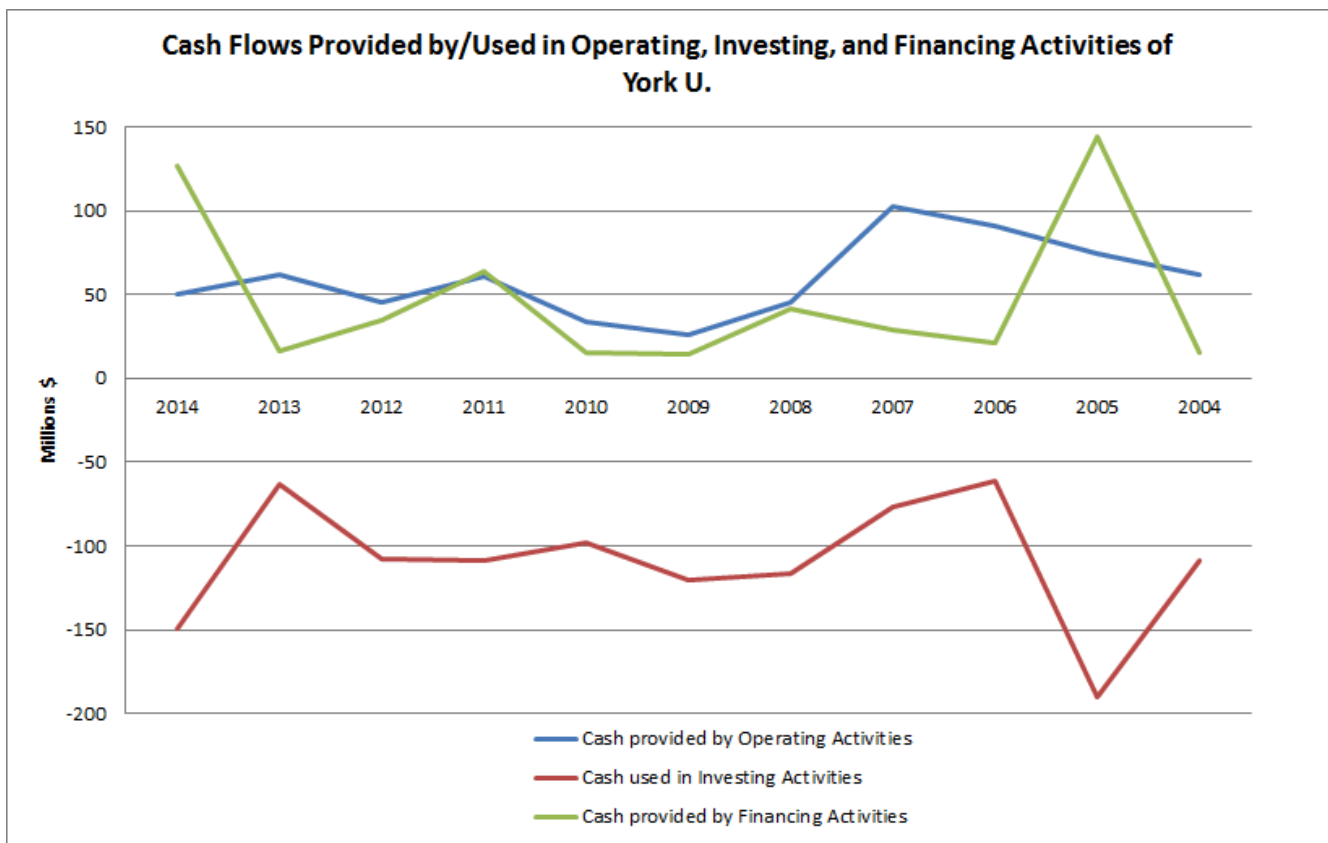
In contrast to the SOP, the SFP is like a snapshot: it provides information about the financial position of an entity at a point in time. The SFP can be represented by the equation $assets - liabilities = net\ worth$. Since this equation always balances, the SFP is also known as the Balance Sheet. To illustrate the SFP equation, if someone owns a house worth \$500,000 but has a mortgage of \$300,000 on it, that person is worth the difference of \$200,000.

- The net worth or net assets of York University have increased from \$264 million in 2004 to \$1,216 million in 2014.

The Statement of Cash Flows (SCF)

Deficits and surpluses on the SOP are the result of numerous estimates and choices made by the management. In contrast, cash from operations is a fact. Therefore, users of financial statements are also interested in knowing what the actual cash flows from operations of an entity are. The SCF provides information about the cash flows from (cash used by) three types of activities: i) operating, ii) investing, and iii) financing. The cash flow from operations section of the SCF provides information about whether the operations of an entity are generating cash surpluses or deficits. As pointed out earlier, in the long-run the operations of an entity should help generate cash to fund not only its day-to-day operations but also pay for its capital expenditures. To give a snapshot of each of these three areas:

- **Operating:** York University has generated a cumulative cash surplus of \$277 million during the 2009-2014 period (\$374 million during the 2004-2008 period). York University has generated adequate cash from its operations to not only comfortably meet all its day to day operating needs but also to handsomely fund steadily increasing capital expenditures over the years. Thus, despite the fact that York University's cash from operations did decrease in the 2009-2014 period as compared to the 2004-2008 period, it is clearly not at the brink of financial disaster.
- **Investing:** The investing section of the SCI provides information about the investing activities of an entity, such as capital expenditures and cash inflows and outflows relating to investments in bonds and shares. York University cumulatively incurred \$647 million in its investing activities during the 2009-2014 period. In contrast, it cumulatively incurred \$553 million in its investing activities during the 2004-2008 period. Thus, despite a drop in cash inflows from operations during the 2009-2014 period, as compared to the 2004-2008 period, York University accelerated its investing expenditures in the 2009-2014 period.
- **Financing:** The financing section of the SCF provides information on the external sources of funding of an entity. More specifically, the financing section provides information on whether an entity is incurring additional debt to meet its operating and investing activities, whether the entity is able to pay off its debt on a regular and timely basis, and contributions received from outsiders that are restricted to be used for capital purposes or as endowments. York University has from time-to-time issued debt, but has also consistently paid of such debt over time. For example, York University issued debentures worth \$99.3 million in 2014. At the same time, during the 2009-2014 period York University repaid \$43.9 million of long-term debt.



Statement of Changes in Net Assets

The last financial statement, the Statement of Changes in Net Assets, provides a reconciliation between the beginning and ending balances of the various funds that make up York University's net assets. The statement also provides information on the amounts transferred between these funds each year. As pointed out earlier, the net assets of York University represent its net worth. York University has maintained three funds since 2009: i) deficit, ii) internally restricted funds, and iii) endowment funds. Until the end of 2008 there was a fourth fund – capital assets – which was collapsed in 2009: the majority balance was reclassified as internally restricted funds, with a relatively small amount being reclassified as part of the endowment funds. The ending balances in these funds add up to the ending net assets balance on the SFP. While the deficit and internally restricted funds are completely unrestricted, the endowment fund has both externally and internally restricted components.

- *Presently, only the endowment funds appear to include funds that are preponderantly externally restricted. Both the deficit fund and the internally restricted funds include funds that have been ear-marked at the discretion of the management of York University, i.e., amounts can be freely transferred from one fund to the other at the complete discretion of the management.*
- For example, during the 2009-2014 period York University transferred \$241.4 million from the deficit fund to the internally restricted funds. York University also transferred a further \$5.9 million from the deficit fund to the endowment funds during this period. It is no wonder that the deficit fund has lived up to its name over the years, racking up deficits year over the year, and ending with a \$(43.1) million balance at the end of 2014.

Notes to the Financial Statements

Finally and importantly it is essential that users read through the notes to the financial statements of an entity to truly understand them. The *notes provide additional details about the accounting methods used* by an entity while preparing its financial statements and about the revenues, expenses, assets and liabilities of that entity. Different entities use different accounting methods to account for similar activities, assets and liabilities. Therefore, users of financial statements should carefully read through the notes to the financial statements provided by an entity to arrive at correct conclusions about the operations and financial position of that entity.

- In 2014 York University choose to early adopt Section 3463 of the CICA Handbook on a retroactive basis. Retroactive means accounting as if the new section was always in place from the very beginning and thus restating previous years' financial statements to be in line with the new section.
- *Section 3463 requires* not-for-profits to include the impact of *the re-measurement of post-employment benefits in the net assets section, instead of the SOP*. The post-employment benefits re-measurement has yielded positive results for York University in 2013 and 2014 to the tune of \$77.5 million and \$197.9 million respectively. Before the introduction of Section 3463 these amounts were required to be shown in the SOP, which would have resulted in considerable surplus on York University's SOP.
- The early adoption of Section 3463 means that York University is showing a much more modest surplus of \$4.4 million for 2014 and a deficit of \$(2.8) million for 2013 on its 2014 financial statements. In contrast, in its 2013 financial statements, before the impact of the adoption of Section 3463, York University showed a surplus of \$58.9 million in its 2013 financial statements.

Further reading

Bill Salatka, 'Analyzing Financial Statements' (Toronto: OCUFA, November 2012)